



## Oil production and refinery

Naftogaz owns shares in **Ukrnafta**, *Ukrasvydobuvannya (UGV)* and *Ukratnafta* which operate in the Ukrainian market for oil, petroleum products and liquefied petroleum gas (LPG). In addition, Chornomornaftogaz owns the rights to a number of assets in oil upstream in Crimea. The company does not currently have access to these assets because of the occupation of the peninsula.

### UGV

#### Oil and condensate extraction

UGV is the largest gas production company in Ukraine and second in the production of oil and condensate: in 2014 the company's share in the total gas production was 68%, and it had a 20% share in crude oil and condensate extraction in Ukraine.

As of the beginning of 2015, the company's operational assets included 2 441 gas wells, 194 oil wells, and 82 drilling rigs. There are presently 139 hydrocarbon fields under development, located in Kharkiv, Poltava, Sumy, Donetsk, Dnipropetrovsk, Luhansk, Lviv, Ivano-Frankivsk, Volyn, Chernivtsi and Zakarpattia regions.

The depletion of the company's initial recoverable reserves at existing fields is estimated at almost 72% in gas, 21% in oil and 63% in condensate.

In March 2015, the parliament increased the royalty rate for oil and gas companies, and for UGV it was set at 70% of revenues to ensure the state has sufficient reserves to finance utility subsidies for households following the gas price hike. The increased royalty rate, albeit introduced for plausible reasons, negatively affects the finances and production rate of UGV and, if extended for a long period of time, can lead to a sharp reduction in the production of oil and gas in Ukraine.

### Refinery

UGV largest refinery facility is Shebelynsky Refinery. In addition, the company has the following refinery capacities: LPG producing Yuliyivska and Tymofiiivska facilities for the advanced extraction of hydrocarbons, the Bazylivschyna plant producing LPG and stabilized gas condensate, the Yabluniv division producing LPG and dry gas, and the Orhovytska plant, which produces bitumen.

UGV is the largest producer of LPG (a mixture of propane and butane) in Ukraine. In 2014, the company produced 187 thousand t of LPG, a 17% reduction compared to 2013. The company also produced 206 thousand t of gasoline (30% less than in 2013), and 118 thousand t of diesel fuel (21% less than in 2013). The production decrease was caused by the reduced extraction of key raw materials.

#### Types of Activities

GAS

OIL

OVERSEAS PROJECTS

INTERNAL PROJECTS

Research and Development Activity

Environmental policy

Occupational health and safety policy

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## Petroleum products supply

UGV covers nearly 4% of the total demand for petroleum products and nearly 21% of the total LPG demand in Ukraine.

The company has a network of 15 filling stations in the Kharkiv region. In 2014, this network sold 5% of the petroleum products produced by UGV. The remaining oil products were sold by the company at public auctions or through direct contracts.

Between June 2015 and April 2016, oil products produced by UGV will be sold through its retail network of filling stations, at public auctions, or through tenders where it will exclusively supply the Defense Ministry, Interior Ministry, Security Service, Foreign Intelligence Service and other government agencies responsible for the military operation, or as prescribed by decrees of the Cabinet of Ministers of Ukraine.

## UKRNAFTA

Naftogaz is the major shareholder in **Ukrnafta**, holding a 50% + 1 stake in the company. However, in 2014 Naftogaz did not exercise control of the company and **Ukrnafta** was not consolidated in the financial statements of the group for 2012-2013 and 2014. The share of Naftogaz in **Ukrnafta** operations is reflected in the consolidated financial statements under 'Investments in associates'.

On 10 October 2014, an extraordinary meeting of the shareholders of **Ukrnafta** approved the distribution of the company profits for 2011-2013. The dividend share of Naftogaz should have been transferred to the state budget. However, the executive body of the company has not fulfilled this decision as of October 2015.

In March 2015, the Verkhovna Rada adopted the law 'On Amendments to the Law of Ukraine On Joint Stock Companies', which reduced the requirements for a shareholder quorum to 50%. Naftogaz is currently examining how this reduction will influence the group's ability to regain control of and, therefore, the consolidation of **Ukrnafta**.

## Oil and condensate extraction

**Ukrnafta** is one of the largest oil and gas companies in the country. In 2014, the company share in oil and condensate extraction was 69%, and it accounted for 6% of gas produced in Ukraine.

As of the beginning of 2015, **Ukrnafta** operated 1 949 oil wells and 185 gas wells and 58 drilling rigs. The company has extraction facilities in Poltava, Chernihiv, Sumy, Kharkiv, Dnipropetrovsk, Lviv, Ivano-Frankivsk and Chernivtsi regions.

The depletion of the company's initial recoverable reserves at existing fields is estimated at almost 83% in oil and 81% in gas.

In 2014, the volume of oil and condensate extracted by **Ukrnafta** decreased by 7% compared to 2013, and amounted to 1 888 thousand t. Production of oil gas reached 449 million cubic meters, which is 7% more than in 2013.

## Refinery

By law, **Ukrnafta** sells crude oil and condensate it extracts through public auctions. Kremenchuk Refinery, which belongs to Ukratnafta (43% owned by Naftogaz), is now the only oil refinery operating in Ukraine.

Because of distorted regulations, in 2014, **Ukrnafta** crude oil was sold with a de facto discount factor, reducing the selling price of oil by 15%. This problem was corrected in January 2015 when the Cabinet of Ministers made appropriate changes to auction regulations.

**Ukrnafta** produces LPG at three processing plants: Kachaniv, Hnidyntsiiv and Dolyna. In 2014 a total of 163 thousand t of LPG was produced, which is 4.8% less than the previous year.

### Petroleum products supply

**Ukrnafta** owns one of the largest networks of filling stations in Ukraine, with more than 500 facilities in most of the regions across the country.

The share of **Ukrnafta** filling stations in the total sales of gasoline and diesel fuel in Ukraine in 2014 reached 15%, and the network had an 18% market share in LPG sales in Ukraine.

LPG **Ukrnafta** sells is mostly of its own production. In supplying gasoline and diesel fuel, the company uses products from external suppliers. The **Ukrnafta** audit committee discovered that in 2014 **Ukrnafta** suffered UAH 800 million in losses in this market segment, primarily because it was buying gasoline and diesel fuel above the market rate.

### EXTRACTION OF CRUDE OIL AND CONDENSATE, PRODUCTION OF PETROLEUM PRODUCTS AND LPG BY COMPANIES WHERE NAFTOGAZ OWNS SHARES, 2014

Company	% owned by Naftogaz	Crude oil and condensate		Petroleum products (gasoline, diesel, fuel oil)			LPG		
		thou-sand t	% of total extraction in Ukraine	thou-sand t	% of total production in Ukraine	% of total consumption in Ukraine	thou-sand t	% of total production in Ukraine	% of total consumption in Ukraine
UGV	100%	533	20%	378	25%	4%	187	42%	21%
Ukrnafta*	50% + 1 share	1 888	69%	-	-	-	163	36%	18%
Ukrtatnafta*	43%	-	-	1 155	75%	14%	63	14%	7%
Total	-	2421	89%	1533	100%	18%	413	92%	46%

\*not consolidated in the financial statements of Naftogaz for 2014

